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I. INTRODUCTION

1. Although inflation has been with the Agency throughout its history, in recent years the astonishingly higher, double-digit inflation rates have become alarming to numerous managers within DD/A as these managers see the rapid erosion of their buying power, with its deleterious effects on plans and programs. The DD/A, also recognizing the problems such inflation places on the Directorate, directed the DD/A Assistant for Resources to establish an Inflation Study Group to examine the impact of inflation within the various offices of the Directorate.

In response, a study group was convened consisting of:

2. For comparability purposes, the budget and personnel statistics in this study represent adjustments of Congressional Budgets from the base year of 1967 onward. These adjustments were necessary because of the various inter-Directorate transfers of functions which have occurred in recent years. Thus, the budget figures presented represent a reasonably accurate picture for comparison purposes.

II. Inflation Impact on the DD/A1. General

Although the Directorate contains nine basic support activities, the problem of assessing inflation was not difficult. The impact has been felt in both main categories of DD/A budgeting areas; "personal services" and "goods and services".

a. Personal Services

Since 1967 the index of costs for personal services has risen 71 percent. Within DD/A, the average cost per employee has risen from \$_____ in 1967 to \$_____ in 1975, a rise of ____%. To partially offset this enormous rise, DD/A has drastically reduced its personnel ceiling over these years, but the reductions have not been able to offset the rising costs as much as management had hoped. In accomplishing the personnel reductions, some programs and services have suffered, and most Offices believe they can no longer absorb personnel cuts and continue fulfilling the responsibilities they are charged with. Fortunately, to date, automation and productivity increases, plus the elimination of some programs, have cushioned the impact of the reductions, but it now appears that only core remains. Further cutting now and in the future will cut core which inevitably will result in serious ramifica-

tions. Although reducing personnel should always be a management goal, reducing personnel to save money without commensurate reductions in functions seems to have nearly reached its limits in DD/A. However, inasmuch as realistic budgeting (budgeting for inflation, which in this context would allow budgeting for pay raises, etc.) is not permitted, there appears to be no alternative to further personnel reductions, unless personal services "underbudgeting" continues and whereby the Agency adopts a policy of attempting to make up personal services fund shortages by use of the "reserve release" option each fiscal year. A consolidated overview of DD/A positions, personal services and goods and services budgets is shown:

b. Goods and Services

- (1) From 1967 ³ ~~until~~ ^{there} 197~~4~~ the index costs of goods

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and services did not rise nearly as rapidly as personal services, but the situation changed drastically in 1974 as the above statistics show. In 1974, prices of goods and services rose 23 percent, impacting severely on Communications, Logistics , where the bulk of goods and services originate. OJCS, the other goods and services oriented Office, was not seriously affected.

(2) As with personal services, the prohibition against budgeting for inflation causes many problems, e.g., contracts are bid much higher than budget estimates contain, much less requisitioning of supplies and equipment can be accomplished because of rapid price rises occurring between the time budget estimates are prepared and the time requisitioning actually occurs, maintenance of buildings and facilities is postponed because funds intended for these purposes must be used to make up for shortages elsewhere, etc.

c. As the above statistics reveal, while the DD/A budget in terms of current dollars has increased \$_____ or _____% since 1967, the constant dollars have declined by \$_____ or _____%. As pointed out earlier, the lower inflation rates of

1967 through 1973 were assimilated by the Directorate through personnel cuts, productivity increases, reductions in some programs, etc. However, the higher inflation rates of recent years causes serious problems and, if inflation continues, and the judgment is that it will over the long run, it will become more and more difficult for the Offices to absorb increased costs and simultaneously maintain essential services.

d. What is the likelihood that inflation will continue? Though the pace of inflation now seems to be easing, some of the policies designed to end the recession now may sustain future inflation. We are already well into FY-1975 and significant rises in costs have already been recorded. Therefore, it appears the average increase in costs of goods and services will be a minimum of 7 to 9 percent for the year. The annualization of the October 1974 Pay Act will produce a modest increase in the index for personal services. For fiscal year 1976, there is growing agreement that the pace of inflation will be between 7 and 11 percent; higher for non-compensation components of the budget and less for personal services. While such magnitudes are modest in terms of the recent

pace of inflation, a 7 percent increase in costs would amount to more than for the 25X1A Directorate. The chances of offsetting such an increase through productivity increases are virtually nil; historically such measures could offset only 2 to 3 percent rises in costs.

e. The deflators applicable to the Agency are given in the budget table, above. They are expressed as separate deflators, one for compensation and one for goods and services. Developed by OER at the request of the Office of the Comptroller, they appear to be a valid measure of the way the Directorate's purchasing power has shrunk as a result of inflation.

2. Specific Impacts on the Offices

Inflation has impacted the Offices in various ways and to differing degrees, depending upon their functions and ratio of personal services costs to costs of goods and services. The individual Office experiences are discussed in detail in the Office Annexes. Discussed below are the highlights of these Annexes, which point out some of the more serious budgetary problems inflation is causing. 25X1C

